Budgeting and Performance Measurement
Learning Objectives

After studying Chapter 13, you should be able to:

- Explain the objectives of budgeting
- Describe methods of integrating planning, budgeting, and performance measurement
- Explain the differences among various budgeting approaches
- Describe the budgeting process for a state or local government
Learning Objectives (Cont’d)

- Identify the procedures involved in specific types of budgets including appropriation budgets, revenue budgets, cash budgets, and capital budgets
- Describe managerial tools used to improve performance and communicate the results of the budgeting process
- Describe the budget and cost issues in grant accounting
Objectives of Budgeting for a Government

- The budget embodies management’s plans to meet public expectations to:
  - Prioritize community program and service goals
  - Authorize the expenditure of resources to meet goals
  - Comply with laws over spending appropriations
  - Improve quality of services in the near term
  - Demonstrate stewardship for public funds in the long-term
Objectives of Budgeting for a Government, (Cont’d)

- Two views of a governmental budget are that they:
  - Demonstrate compliance with laws and regulations
  - Communicate performance effectiveness
GASB Budgeting, Budgetary Control, and Budgetary Reporting Principle (see Chapter 2) provides that:

- An annual budget should be adopted
- The accounting system should provide the basis for appropriate budgetary control
- Budgetary comparisons should be included in the financial statements for the funds for which an annual budget has been adopted
Budgeting Principles (Cont’d)

- Budgeting comparison schedules should be presented as RSI and include:
  - The original budget
  - The final appropriated budget
  - Actual inflows, outflows, and balances

- Stated on the government’s budgetary basis
The budget can communicate accountability for the use of public funds and strategies for improving the quality of government services.

GFOA criteria for the Distinguished Budget Presentation Award relates to the budget as a:

- Policy document
- Financial plan
- Operations guide
- Communications device
A budget to actual comparison is required supplementary information.

It can be presented as:

- A statement in the general purpose external financial statements, or
- A schedule after the notes to the financial statements.
Integration of Planning, Budgeting, and Performance Measurement

A “managing for results” process helps focus attention on how the following activities can lead to meeting goals (such as safe highways, healthy children, thriving communities):

- Strategic planning
- Program activity planning
- Measuring for results
- Budgeting for results
- Managing work processes
- Evaluating results
- Reporting results
Results-Oriented Performance Measurement System

- Requires clear identification of:
  - Outputs (e.g., number of lane-miles of road repaired, number of serious crimes reported)
  - Outcomes (e.g., percentage of lane-miles of road maintained in excellent condition, percentage of residents rating their neighborhood as very safe)

- Critical components include:
  - Transparency
  - Measures over time
  - Measures in a variety of activities
  - Leadership support
Various Budgeting Approaches

- Line-item budgeting (incremental and zero-based)
- Performance budgeting
- Program budgeting (and PPBS)
- Entrepreneurial budgeting (e.g., using balanced scorecards)

Note: governments seldom choose a single budgeting approach, rather entity-wide budgets are constructed using different approaches
Incremental Budgeting

- Simple and widely used
- Derived from the prior year’s budget
- Focuses on departmental expenditures by applying a percentage increase “across the board” to all line-items
- The increase may be the annual rate of inflation, or specific adjustments that relate to expected salary increases or shrinkage relating to scaling back operations
- Doesn’t relate inputs to outputs or outcomes
Zero-Based Budgeting (ZBB)

- Requires that the very existence of each activity be justified each year, as well as the amount of resources that will be allocated to it.
- Uses readily available objects-of-expenditures.
- Easy to understand and common agreement that programs should be re-evaluated annually.
- Not widely used as it is time-intensive and skepticism arises when marginally successful programs continue to be funded.
Performance Budgeting

- A plan for relating resource inputs to the efficient production of outputs
- Moves from a legal view of the budget that is a plan of estimated expenditures to a business view of the budget as an operating plan
- Introduced in 1949 by the Hoover administration
- Evolved as government managers became more professional and adapted business techniques
Program Budgeting

- Discloses the full costs of programs or functions without regard to the number of organizational units that might be involved.
- Often considered synonymous with performance budgeting; however, that method typically focuses on the relation between inputs and outputs of each organizational unit, rather than programs.
Planning-Program-Budgeting System (PPBS)

- Comprehensively integrates planning and control into one system
- Provides legislators and public administrators with output-oriented information that can be used in evaluating how successful the government is in meeting strategic objectives
- Developed in the 1960s at the federal level
- Advantages include the ability to address whether the government is better off operating certain programs
Entrepreneurial Budgeting

- Approaches budgeting at the highest level in the government, not as a traditional accounting task
- Merges strategic plans, incentives, and accountability into the budget
- Communicates budget information to citizens
- A balanced scorecard is an entrepreneurial tool that links financial and nonfinancial indicators to share with governing bodies
Budgeting Process

- **Budget calendar** - schedule of activities in the process including public hearings to ensure participation by all

- **Budget officer** - person responsible for providing technical assistance to operating personnel who prepare the budgets
Budgeting Appropriations

- Administration’s requests for authorization to incur liabilities for goods, services, and facilities
- Governments budget expenditures required to meet public demand for services first, followed by the budget for revenues to fund those expenditures
- Conflicts and competing demands from various stakeholder groups must be resolved by the chief executive in budgeting appropriations
The revenue budget is the plan for financing proposed appropriations

- Budget for sources of inflows of financial resources, including revenues, interfund transfers, debt issue proceeds
- Sources of revenues may be controlled by state or local laws and ceilings, e.g., limits on property tax rates and assessments
Develop multi-year budgets for capital expenditures that are expected to benefit more than one period, e.g., land, buildings, and equipment

- Capital improvement plans include:
  - improvement of streets
  - construction of bridges and buildings
  - acquisition of land for recreational use, parking lots, future building sites
  - urban renewal
Budgeting Cash Receipts and Disbursements

- It is critical to foresee the effects of operating plans and capital improvement plans on cash.
- Governments should have sufficient cash on hand to meet current liabilities (e.g., payroll and suppliers).
  - Tax anticipation notes are short-term borrowings usually from banks that are repaid when taxes are collected.
  - Sweep accounts are used to automatically invest any daily excess of cash over target levels.
- Accelerate cash receipts with early billing, payment discounts, late payment penalties, use of lock boxes, and credit card and electronic payments.
Several business techniques have been adapted by governments to improve the efficiency of operations and reduce the need for higher taxes:

- Total quality management (TQM)
- Customer relationship management (CRM)
- Service efforts and accomplishments (SEA)
- Activity-based costing (ABC)
- Balanced scorecards
Total Quality Management (TQM)

links customer satisfaction (taxpayer and other resource providers) to improvements in the operating systems and processes used to provide goods and services
Elements of a TQM System

- Support of top-level officials
- Customer orientation
- Employee involvement
- Rewards for employees’ improvement
- Training provided to employees
- Reduction of barriers to productivity
- Productivity and quality measures
- Written mission statements leading to targets
Customer Relationship Management (CRM)

- CRM systems create an integrated view of a customer to coordinate services from all channels of the organization.

- The purpose is to improve the long-term relationship the organization has with its customer.

- Governments are finding CRM systems helpful in managing services provided to citizens over time.
SEA measures fall into three categories:

- Service efforts (resources used)
- Service accomplishments (outputs and outcomes)
- Those that relate service efforts to accomplishments
EXAMPLE:
SEA Measures in a Police Department

- **Service efforts** - number of police employed and dollars paid to them

- **Service outputs** - number of patrols responding to calls or investigations

- **Service outcomes** - reduction of deaths and thefts, level of safety felt by citizens
Activity Based Costing (ABC)

- ABC traces the cost of specific process-related activities to specific outputs of goods and services.
- In ABC, resource “cost drivers” replace the traditional step-down allocations of indirect costs with cause-and-effect relationships at the activity level.

COSTS → DRIVERS → OUTPUTS
Balance Scorecards

- An integrated set of financial and nonfinancial performance targets
- Measures are classified into groups:
  - **Financial** - Has our financial performance improved?
  - **Customer** - Do customers recognize that we are delivering more value?
  - **Internal business processes** - Have business processes improved so we can deliver more value?
  - **Learning and growth** - Have we maintained our ability to adapt and improve?
Grant Accounting

Budgets for grants requesting funding generally include:

- A statement of program purpose
- A needs assessment
- The process to be employed to conduct the program
- A program evaluation process
- Credentials of the principal investigators
- A timeline over which the goals of the program will be accomplished
- A budget detailing how the funds will be spent
Allowable Costs for Federal Grants

Cost principles governing payments to recipients of federal funds are found in:

- *OMB Circular A-87* for state and local governments
- *OMB Circular A-21* for educational institutions
- *OMB Circular A-122* for not-for-profit organizations
Allowable Costs in Federal Grants (Cont’d)

- **Allowable costs** are those that are necessary and reasonable for efficient performance of the federal award, such as, compensation of employees, cost of materials, and depreciation.

- **Unallowable costs** include alcoholic beverages, bad debt expense, and salaries of the chief executive officer.
Governments may continue to prepare budgets to demonstrate compliance with laws and regulations.

Other governments have adapted business management practices and integrated the budgeting and performance measurement tasks.

Under either view, communication of compliance and performance information to stakeholders about the effectiveness of the government is essential.

END